

SENATE BILL REPORT

SB 5936

As of February 24, 2005

Title: An act relating to the preservation of claim rights of a contractor, subcontractor, or supplier on construction contracts.

Brief Description: Limiting the effect of construction contract provisions affecting the claim rights of contractors.

Sponsors: Senators Kastama, Rockefeller and Esser.

Brief History:

Committee Activity: Government Operations & Elections: 2/22/05.

SENATE COMMITTEE ON GOVERNMENT OPERATIONS & ELECTIONS

Staff: Mac Nicholson (786-7445)

Background: Construction contracts may contain mandatory protest and claim provisions to address certain situations that may arise during the course of construction. Such clauses generally require the contractor to follow specific notice requirements when seeking additional payment for increased expenses incurred. Such clauses may be used in public works contracts as well as private contracts.

In 2003, the State Supreme Court had occasion to interpret such a clause in *Mike M. Johnson, Inc. v. Spokane County*, 150 Wn.2d 375. In that case, Mike M. Johnson (MMJ) was the contractor in a sewer construction project. During construction, MMJ encountered buried phone lines that halted work while the utility conflict was resolved. The contract contained specific and detailed procedures for claims of additional compensation, time extensions, and changed conditions. However, the court found that while MMJ did submit several letters claiming it was owed additional compensation, MMJ did not submit a formal claim as required in the contract.

The court ultimately upheld dismissal of the case on a summary judgment motion. The court noted that as a general matter of contract law, procedural contract requirements must be enforced absent either a waiver by the benefitting party or an agreement between the parties to modify the contract. The court rejected MMJ's argument that when an owner has actual notice of a contractor's claim, that notice excuses compliance with mandatory contractual claim provisions. Rather, the court held that actual notice is not an exception to contract compliance and that a waiver of a contract provision must be made by the party benefitting from the provision.

The dissent in *Mike M. Johnson* agreed that actual notice is not an exception to contract compliance. However, the dissent asserted that the real issue is whether the county's actual notice plus its direction to the contractor to proceed amounted to compliance with the contract by the contractor or waiver of the notice requirement by the county. The dissent asserts that

the rule should be that when an owner directs a contractor to do work outside the original contract, and then observes the work being done, the owner cannot then rely solely on technical non-compliance with a claim provision to deny reasonable compensation, especially when the owner has not been prejudiced by the non-compliance.

Some public agencies use construction contracts that contain protest and claim provisions that may allow a contractor to pursue a claim even though the contractor has failed to make the required notice. These provisions state that failure to give the required notice constitutes a waiver of the contractor's rights unless the contractor can prove the owner's interest was not prejudiced in any way.

Summary of Bill: Any clause in a construction contract that purports to waive, release, or extinguish the claim rights of a contractor to damages or an equitable adjustment based on failure to submit claim notice or claim related documentation in a specified time frame or form is enforceable to the extent that the party failing to receive such notice was prejudiced.

Appropriation: None.

Fiscal Note: Not requested.

Committee/Commission/Task Force Created: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Testimony For: Contractors will be driven out of business unless this bill is passed. The Mike M. Johnson case imposed a death penalty on contractors who don't comply with complex and technical notice and claim requirements. Without the bill, contractors will have to incur additional costs because they will have to bring in attorneys to make sure that notice provisions are met. Owners are making notice and claim provisions hyper-technical and difficult to comply with in the hope that contractors will fail to meet them and therefore cannot seek additional compensation. Contractors who don't meet technical notice and claim provisions are prevented from being compensated for their work even where the owner directs the contractor to go ahead with the work. The bill just re-establishes a more equitable solution.

Testimony Against: The Mike M. Johnson case just upheld 90 years of case law and provided that contract notice provisions are enforced absent waiver. The bill operates to eliminate summary judgment in all cases which will force the owner to go to trial to establish prejudice. Prejudice is undefined in the bill and passage of the bill will spawn litigation regarding what prejudice is and how it is proved. Notice provisions are in the contract in advance and contractors can negotiate different terms. The notice and claim provisions provide a way for the owner to manage the project for the public, including keeping the project on budget and on schedule. Taking away that power is bad policy. Existing law prevents an owner from demanding and observing extra work and then failing to compensate, so there is no risk that a contractor will not be paid for such work.

Who Testified: PRO: Michael Transue, Associated General Contractors; Paul Cressman and Bruce Cohen, Short, Cressman and Burgess; Andy Ward, Valley Electric.

CON: Dick Prentke, Perkins Coie; Pete Wall and Lorraine Wilson, Tacoma Public Schools; Linda Shilley, Port of Tacoma.